IU International

1978 Annual Report to Investors

IU International

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This Is IU International

IU International Corporation is a diversified company serving land transportation, ocean shipping, utility services, industrial products and services, distribution services, and agribusiness markets.

IU evolved from a utilities holding company founded in 1924 as International Utilities Corporation. Following several years of diversification, the name was changed in 1973 to IU International Corporation.

Today, IU is a worldwide operating company with 42,000 employees and 45,000 shareholders.

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1105 North Market Street
Wilmington, Delaware 19801
302 652-1121

Executive Offices
1500 Walnut Street
Philadelphia, Pennsylvania 19102
215 985-6600

Financial Highlights

In thousands, except per share data

	1978	1977*
Revenues	**$2,567,316**	$2,285,900
Net earnings	**$12,060**	$58,876
Earnings per share	**$.30**	$1.74
Dividends per common share	**$.925**	$.90
Shareholders' equity per share	**$18.11**	$19.08
Total assets	**$2,793,474**	$2,704,013

*Restated for the accounting changes described in Significant Accounting Policies on page 24.

To Our Shareholders:

Most of IU's operations performed well in 1978, but a decision to reduce our exposure in ocean shipping led to sharply lower net earnings.

Net earnings for 1978 were $12.1 million, or 30 cents per share, on revenues of $2.57 billion. Without the fourth quarter special charges, IU's 1978 net earnings would have been $1.97 per share, including 20 cents in foreign currency adjustments. In 1977, IU earned $1.74 per share (restated), including 29 cents in currency adjustments, on revenues of $2.29 billion.

In 1978, IU paid a dividend of 92.5 cents per common share, up from 90 cents in 1977. This increase marks the 34th consecutive year of rising dividend payouts—a record that began when the present class of common stock was first issued in 1944. We expect to continue IU's long-standing dividend policy. The indicated dividend payout for 1979 is 95 cents per common share.

In January 1979, we announced several actions that will improve IU's future position despite the negative impact on 1978 reported net earnings. These included cancellation of an order for one liquefied natural gas (LNG) carrier and further reduction of the crude oil tanker fleet. The cancellation, reductions, and related tax adjustments penalized IU's earnings by $55.6 million, or $1.67 per share. This was done to reduce the capital obligations and projected tanker losses of Gotaas-Larsen Shipping Corporation.

The timing of the cancellation was related to the turmoil in Iran as well as the United States government's rejection of two pending LNG import projects. The decision to lessen our financial exposure in crude oil tankers was motivated by the continued world surplus of tanker capacity that has depressed shipping rates and pushed the projected recovery of the industry into the 1980s. We have reduced the oil tanker fleet from 17 to six vessels during the past year, keeping only those vessels that can contribute the most to Gotaas-Larsen's results when the tanker market recovers.

Operating earnings improved in 1978 from Gotaas-Larsen's passenger cruise ships, drilling rigs, chemical carriers, and LNG operations.

The special charge to earnings also tends to obscure the good performance of most IU subsidiaries, including especially strong results by the land transportation and utility groups. Four of IU's seven reporting groups had higher operating earnings in 1978, and one was approximately even with the previous year. Only two groups, shipping and agribusiness, had significantly lower results.

IU's land transportation group had record results, with a 33% improvement in operating earnings on a 25% gain in revenues. Our trucking subsidiaries, Ryder Truck Lines and Pacific Intermountain Express, each rank among the six largest motor carriers in the United States. Effective expansion programs and superior customer service have led to increased market shares for both companies. The 1979 outlook for our truck lines is somewhat uncertain as a result of the possible delay in rate relief following the Teamsters' settlement expected this spring, and rate rollbacks proposed by the Interstate Commerce Commission.

Comparison of Earnings

In millions	1978	1977
Contributions by markets:		
Utility services	$ 93.2	$ 78.3
Land transportation	59.5	44.7
Ocean shipping	(7.2)	34.4
Industrial products and services	31.2	31.4
Distribution services	9.6	3.5
Agribusiness	1.6	19.2
Other	13.9	5.1
Operating earnings	201.8	216.6
Corporate expenses, debt expense, and minority interest	(148.8)	(133.6)
Foreign currency adjustments	11.0	14.4
Income taxes	(51.9)	(38.5)
Net earnings	**$ 12.1**	**$ 58.9**

Utility services also produced record results in 1978. Canadian Utilities Limited, whose subsidiaries supply electric power and natural gas to customers mainly in Alberta, had another fine year. The electric utility increased its operating earnings by 14%, while the gas utilities had a 26% increase. In the United States, General Waterworks Corporation continued to upgrade its properties and posted an 18% gain in operating earnings.

IU's industrial products and services companies almost equaled their 1977 earnings, despite strikes that disrupted production at Southwest Fabricating & Welding Company and at Hills-McCanna Company. Excellent earnings from International Mill Service's worldwide metal recovery and materials handling operations and from IU Conversion Systems' environmental protection services nearly offset lower results in the manufacturing units.

Distribution services showed improved results in 1978. Biggers Brothers, a distributor of food products for restaurants and institutions in the Southeast, had its best year. Unijax, a distributor of paper products, recorded moderately higher earnings. The industrial distribution subsidiaries had mixed results, while the dental supply company had a loss.

Agribusiness operations had a difficult year. C. Brewer and Company, Limited, reported losses in sugar and potatoes; wrote off an agronomics investment in Iran; and suffered severe wind damage to orchards in Guatamala. As a result, operating earnings were just above breakeven, with a loss after taxes. One major negative factor was removed when sale of the potato operations in Oregon was completed in January 1979.

Without federal action to stabilize sugar prices, United States sugar growers may not survive. For three years, the dumping of surplus foreign sugar into the American market has kept prices below domestic costs of production. The need to maintain a viable sugar industry under troubled world trade conditions is expected to cause the Administration to provide some relief to Hawaiian and mainland sugar growers in 1979.

On August 14, 1978, C. Brewer became a wholly-owned subsidiary of IU, which had owned approximately 54% of the Hawaii-based company

since 1969. Former C. Brewer shareholders now hold the IU $1.36 convertible preferred stock.

In October, $100 million in preferred stock was placed privately with a Canadian institution by an IU finance subsidiary. This is the largest single equity financing in the company's history. These securities, with an average life of 10 years, pay a floating rate dividend. Proceeds have been used to retire debt and improve liquidity. At year-end, unused bank credit lines exceeded $300 million.

Capital expenditures in 1978 were $248.6 million. We plan to spend about $343 million in 1979, chiefly to support the growth of our utility services in Canada, land transportation companies, and industrial operations. These capital requirements will be met from internally generated cash and through financings at the operating subsidiary level.

Mr. Christy (left) and Mr. Seabrook

Shareholders who study the detailed financial statements will observe that in 1978 when net earnings declined to $12.1 million, income taxes were $51.9 million. In 1977, when net earnings were $58.9 million, income taxes were $38.5 million. The 1978 income tax rate is 81.2%, compared with the 1977 tax rate of 39.6%. This is because IU's total income was substantially higher in 1978 from the non-shipping segments of the business, which are taxable, but net earnings were reduced by special shipping charges, for which only partial tax recovery is possible.

Had it not been for shipping and sugar, IU would have had a good year in 1978. We believe that the actions we have taken in shipping have set it on a good course for the future. C. Brewer also is beginning to respond, and in 1979 we expect the profitable operations to more than offset the anticipated losses from sugar. The other segments of IU should all do well in 1979, so we are expecting a good year.

On behalf of the directors and officers, we commend our 42,000 employees for their dedicated efforts and thank our 45,000 shareholders for their continued support.

Sincerely,

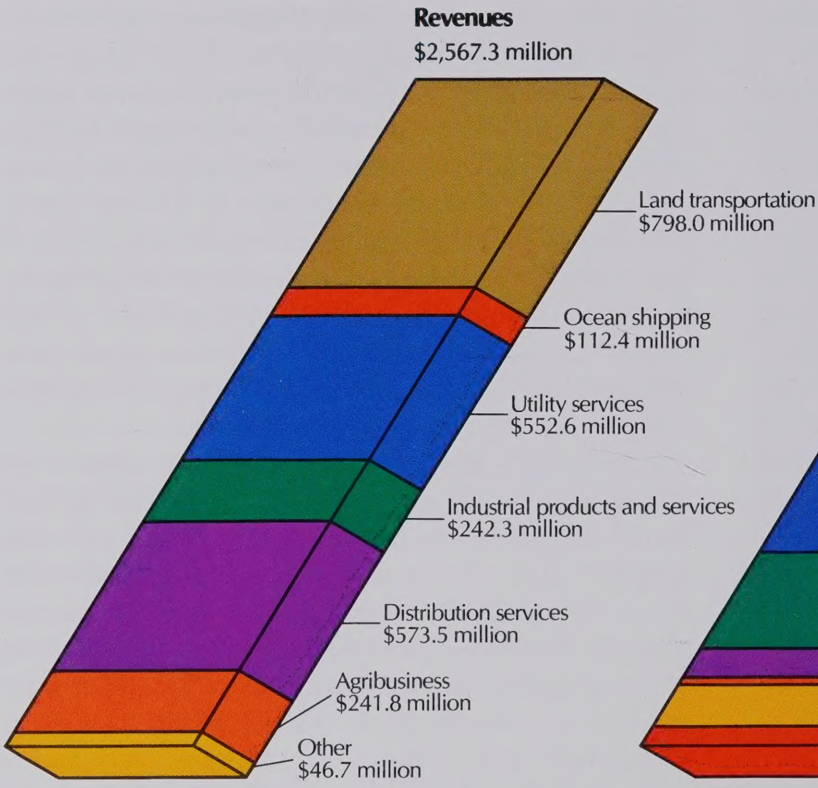
John M Seabrook

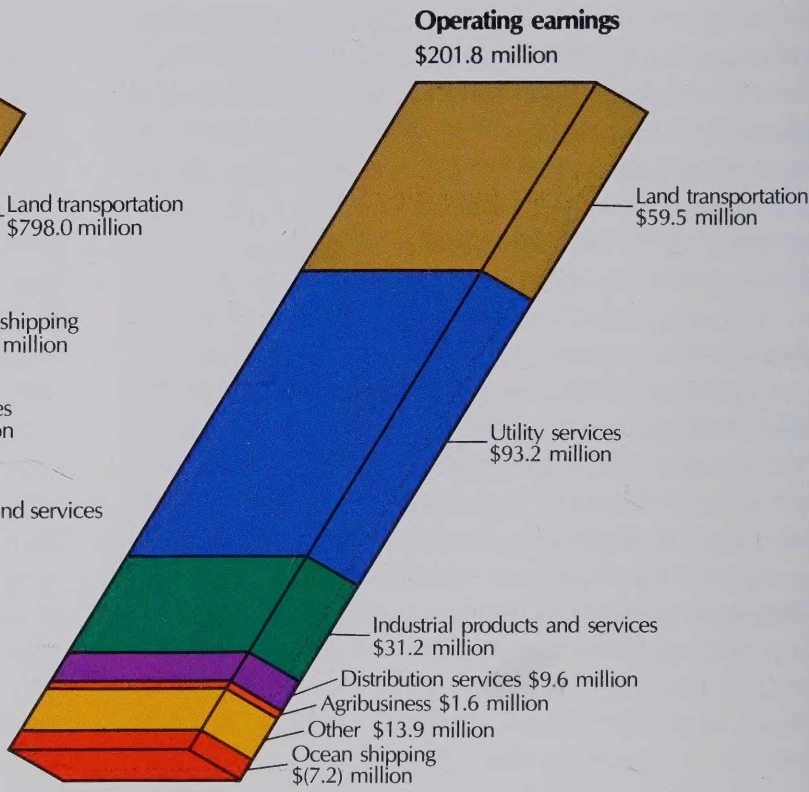
John M. Seabrook
Chairman

John Gilray Christy

John Gilray Christy
President

March 5, 1979





IU's senior officers are (from left) John B. Turbidy, executive vice president; John T. Jackson, chairman of the executive committee; James J. Burke, executive vice president; and Robert F. Calman, vice chairman of the Board.

Land transportation

Land transportation operations produced record results again in 1978. Revenues increased to $798.0 million, up 25% from $637.6 million in 1977. Operating earnings climbed to $59.5 million, an increase of 33% over the $44.7 million reported a year earlier.

Revenue and earnings growth rates at Ryder Truck Lines and Pacific Intermountain Express (P-I-E) substantially outperformed the industry averages. Both truck lines' general and special commodities divisions produced healthy gains, reflecting their ability to attract greater volume and win new customers. Ryder transported 6.0 million tons of freight across a total of 279.6 million miles during 1978, up from 4.9 million tons transported across 230.9 million miles in 1977. P-I-E carried shipments totaling 4.9 million tons over 198.7 million miles during 1978, compared with 3.8 million tons over 170.8 million miles in 1977.

IU's strategy for growth in land transportation continued on the same successful course, expanding service within existing territories and entering new markets. Ryder established a Caribbean division to offer through service for shipments between the United States mainland and Puerto Rico, and acquired new authority to serve West Virginia, Kentucky, and parts of North and South Carolina, Georgia and Texas. P-I-E acquired new authority to serve Albuquerque, El Paso, Dallas, Fort Worth and Vancouver this year.

To support continued growth, Ryder opened 16 new general commodities terminals during the year for a total of 211 terminals at year-end. P-I-E opened 12, for a year-end total of 125 general commodities terminals.

Entering 1979, the entire trucking industry faces three potentially troublesome matters: expiration of the Teamsters' contract on March 31, persistent proposals for deregulation of trucking, and actions by the Interstate Commerce Commission (ICC) that would sharply reduce freight rates.

A timely and equitable settlement of the labor negotiations would serve the best interests of trucklines and their employees, shippers and their customers, and the public in general. Any delay in rate relief following a new Teamsters contract will affect 1979 results.

Deregulation proponents have been intensifying their efforts to change the rules that govern interstate trucking. Although the deregulation issue probably won't be settled this year, the ICC appears eager to change accepted practices in the industry. As presently proposed, deregulation probably would cause economic harm to small- and medium-size shippers but increase the profitability of those very large businesses that can exercise their economic power to demand lower rates or can afford to operate their own trucking fleets. The effects of deregulation on the motor carrier industry are uncertain, but large carriers with well-developed systems probably would survive and flourish.

Both P-I-E and Ryder already have demonstrated a talent for adapting to new business conditions. Both have the management and high service reputation to compete successfully in a deregulated market and perhaps, after some interim uncertainties, even benefit from deregulation if it should come to pass.

Ryder Truck Lines, fourth largest motor carrier in the United States, serves customers concentrated in states east of the Mississippi River and in the Southwest.

The long-term outlook for Ryder and P-I-E is very bright because of their ability to meet the challenges of a changing business environment and grow with the long-term expansion of the North American economy.

Ocean shipping

Gotaas-Larsen Shipping Corporation, IU's ocean shipping subsidiary, had revenues of $112.4 million in 1978, compared with $158.1 million in 1977. After a fourth-quarter charge against earnings resulting from fleet reductions, an operating loss of $7.2 million resulted for 1978, compared with operating earnings of $34.4 million a year ago.

Results from most operations improved. Without the year-end charge against earnings, Gotaas-

Pacific Intermountain Express is the nation's sixth largest truck line. Routes extend from coast to coast and north into British Columbia.

Larsen would have reported higher operating earnings than in 1977.

Included in the year-end charge were provisions for cancellation of a liquefied natural gas (LNG) carrier and further reductions of the crude oil tanker fleet. In addition, delivery of a second LNG carrier on order was deferred for four years.

Subject to approval by the Japanese government, Gotaas-Larsen will incur a cancellation charge of $26.9 million on an LNG carrier, included in the fourth quarter adjustments. Ordered in 1973, this ship on delivery would have cost about $200 million at current exchange rates. Timing of the cancellation of this ship, along with deferral of the other LNG carrier to the end of 1982, was related to the political turmoil in Iran, which disrupted the scheduling of significant gas exports from that country over the near term. In addition, in December 1978, the United States government denied two major LNG import applications. Ocean transportation of LNG will inevitably play an important role in meeting world energy needs, but it has become increasingly obvious that the LNG market will develop at a slower pace than was anticipated when these LNG carriers were ordered in 1973.

The payment terms for the deferred LNG vessel, which are also subject to approval by Japanese authorities, now include protection against fluctuations in the dollar-yen exchange rates.

The remaining charge against Gotaas-Larsen's 1978 operating earnings is related to a provision for a further reduction of the tanker fleet, which continues to produce losses because of a world surplus of tanker tonnage. During the past year, Gotaas-Larsen has reduced its oil tanker fleet to

Cruises have become so popular that "Song of Norway" was enlarged to accommodate more passengers by adding a new section amidships.

six ships. Preliminary agreement has been reached for the sale of an ultra large crude carrier, now in layup; the estimated loss on the sale is included in the 1978 earnings adjustments. Gotaas-Larsen also has charged against 1978 earnings the remaining obligation on a chartered-in tanker, presently in layup.

When these actions are completed, they will significantly strengthen the future cash flow of Gotaas-Larsen.

Remaining in the fleet will be four very large crude carriers and two smaller tankers. The two smaller tankers are on charters expiring in 1981. One of the large tankers is trading in the spot market; two have charters expiring this year; and the fourth is chartered until 1980. In addition to these crude oil tankers, Gotaas-Larsen also operates a fleet of four very modern chemical tankers, each of which is equipped to carry more than 30 separate parcels of chemicals or refined products in special tanks.

Greatly improved operating earnings were recorded by LNG carriers, passenger cruise ships, and drilling rigs. Dry bulk carriers and chemical carriers had somewhat better operating earnings than in 1977. Losses widened in the crude oil tanker division, largely offsetting improvements recorded elsewhere.

LNG operations produced strong results during 1978, principally because three vessels are chartered for 20 years to transport gas from Abu Dhabi to Japan. The company's fourth LNG carrier was employed for several months in 1978, but was in layup at year-end. Further short-term employment opportunities are under discussion. LNG operations as a whole should be profitable in 1979.

Each of Gotaas-Larsen's four chemical carriers can transport cargoes ranging from acids to petrochemicals in up to 39 segregated tanks.

Gotaas-Larsen's chemical carriers, with rates improving, introduced regular transatlantic service between North America and western Europe, and the outlook for profitable business is good.

Drilling rig results improved in 1978 because of North Sea exploration, although one of the company's four drilling rigs was idle at year-end due to the usual winter slump in rig utilization there. The long-term outlook is for increased drilling activity in the North Sea, and Gotaas-Larsen's rigs should benefit.

Exceptional results were achieved by cruise vessels in 1978. Growing popularity of cruise vacations led to record occupancy levels during 1978. Advance bookings in 1979 continue at a high level. To meet rising demand, Royal Caribbean Cruise Line, in which Gotaas-Larsen holds a one-third interest, increased accommodations aboard the "Song of Norway" from 880 passengers to 1,040 by adding a new mid-section that resulted in a longer and more spacious vessel. The company considers the lengthening project so successful that a sister ship, the "Nordic Prince", will be enlarged in 1980. Eastern Steamship Lines, which is 100%-owned, is also benefiting from the continuing upsurge in the cruise business.

Looking ahead, Gotaas-Larsen should have sound long-term prospects for its diversified shipping operations, and the company now is in a better position to realize these prospects.

Utility services

In 1978, IU's utility services group had revenues of $552.6 million, up 23% from $448.9 million in

Canadian Utilities began operating this $40 million ethane plant in Alberta in 1978 in a joint venture with Dome Petroleum Limited.

1977. Operating earnings reached $93.2 million, compared with $78.3 million last year.

All of IU's utility businesses reported improved results. The companies include 60%-owned Canadian Utilities Limited, whose subsidiaries supply natural gas and electricity to customers principally in the province of Alberta, and wholly-owned General Waterworks Corporation, which is one of the largest private water service companies in the United States.

Gas service revenues rose to $386.4 million in 1978 from $299.6 million a year earlier; operating earnings were $33.3 million, compared with $26.4 million in 1977. Electric service revenues were $101.5 million, up from $88.5 million in 1977, and operating earnings increased to $38.9 million from $34.1 million.

Following two winters of unusually mild temperatures, typically colder weather returned to Alberta and resulted in increased gas consumption and improved earnings at the gas utilities.

Rate increases, approved in 1977 and 1978, enabled Canadian Utilities' subsidiaries to attain rates of return established by the Alberta Public Utilities Board. Improved earnings also reflect the company's growing investment in capital facilities needed to keep pace with the province's expanding population and demand for services.

During the year, production began at a $40 million ethane extraction plant in Edmonton, Alberta. A joint venture of Canadian Utilities and Dome Petroleum Limited, the facility contributed to 1978 earnings and is continuing to perform according to expectations.

The electric utility's plans for a new coal-fired generating station at Sheerness progressed during the year. In January 1979, the Alberta Energy Resources Conservation Board announced that it would recommend construction of the power station to the provincial government, with the first of two 375-megawatt units scheduled to begin operating in 1985.

Alberta's economic growth rate is the highest in Canada. With more residents and new investments in industrial and commercial projects, the province will provide a healthy environment for the continued growth of Canadian Utilities.

Results at General Waterworks Corporation also improved in 1978. Water utility properties in 14 states produced revenues of \$64.7 million, compared with \$60.8 million in 1977. Operating earnings were \$21.0 million, up from \$17.8 million a year earlier.

General Waterworks continued to improve the overall efficiency and profitability of its properties through effective cost control, a program of rate relief, and consolidation of its resources into its most profitable operations. During 1978, seven operations were sold and 11 were acquired. These programs will continue in 1979 and are expected to provide the foundation for increased profitability in the future.

Industrial products and services

IU's industrial products and services group reported revenues of \$242.3 million in 1978, up from \$224.1 million in 1977. Operating earnings were \$31.2 million, compared with \$31.4 million.

IU's industrial manufacturing subsidiaries, Southwest Fabricating & Welding Company and Hills-McCanna Company, suffered from margin pressures as well as strikes that trimmed revenues and earnings for the year, but continued growth was reported by the two major industrial service companies, International Mill Service (IMS) and IU Conversion Systems.

IMS provides metal recovery and materials handling services for steel mills at more than 70 locations worldwide. Operations at 35 locations in the United States and Canada produced sharply improved results during 1978, and international operations at 36 locations in Europe and Latin America recorded even stronger growth. The economies of most industrial nations expanded in 1978, and steel production rose at mills served by IMS. Additionally, IMS has enlarged its range of services to broaden its revenue base. Steel demand is expected to vary by country in 1979, but the geographic diversity of IMS operations and the

International Mill Service operates at more than 70 steel mills worldwide. This slag processing unit serves a mill in France.

IU Conversion Systems stabilized tons of sludge from a coal-burning electric utility's smokestack scrubber to build this Pennsylvania road.

company's ability to obtain new contracts provide the foundation for excellent performance. Work is under way on IMS' first contract in Egypt, with operations expected to begin during the third quarter of this year.

IU Conversion Systems (IUCS) has demonstrated its ability to transform technology into a profitable service. IU formed this subsidiary in 1972 to complement our other work in the rapidly developing environmental protection market, and growth has been impressive. Marketing both its services and its technology, the company treats pollutants from smokestack scrubbers at coal-burning power plants and industrial wastes from manufacturers. During 1978, two new contracts were awarded to IUCS and six more were obtained in the first weeks of 1979. Now a leader as well as a pioneer in its field, this subsidiary has a broad base for further growth in 1979.

Profitability at G. & W. H. Corson, America's oldest limestone producer, was lower in 1978, but particular emphasis has been given to productivity improvement, which should aid results in 1979.

At Southwest Fabricating & Welding, one of the leading pipe fabricators in the nation, a 14-day strike affected results. At Hills-McCanna, an important manufacturer of ball, diaphragm and butterfly valves, a 27-day work stoppage reduced both revenues and earnings. Delays in a plant expansion program also handicapped results.

The manufacturing subsidiaries entered 1979 with a backlog in excess of $210 million. This backlog, coupled with new manufacturing capacity in place at both Hills-McCanna and Southwest

Biggers Brothers is the Carolinas' leading distributor of foodstuffs for schools, hotels, restaurants, hospitals and other institutions.

C. Brewer's National Molasses subsidiary is the world's largest manufacturer and distributor of molasses-based feed supplements.

Fabricating, should lead to better results in 1979, despite continued pressure on margins in a highly competitive environment.

Distribution services

IU's distribution services companies produced revenues of $573.5 million in 1978, up from $544.3 million in 1977. Operating earnings rose to $9.6 million from $3.5 million in 1977.

IU's distribution subsidiaries include Unijax, a major southeastern paper distributor; Biggers Brothers, a leading distributor of wholesale food products in the Carolinas; Codesco, a supplier of dental products, equipment, and laboratory services; and three industrial distribution companies, Taylor Engineering Corporation in Michigan, The Gage Company in Pennsylvania, and Electric Supply Corporation in Illinois.

Results in distribution services were mixed in 1978. Biggers Brothers was the best performer, with excellent gains in revenues and operating earnings. Unijax, with a well-established market position, reported good revenues and earnings gains, as did The Gage Company and Electric Supply. Losses were reported by Codesco and Taylor Engineering.

IU's plans in distribution services call for continuing emphasis on upgrading or consolidating marginal operations. During the past two years, this program led to closing of the fabricating operation at Taylor Engineering, significantly reducing overhead; sale or closing of three regional industrial distributors in the Southeast and Midwest; consolidation of three institutional food warehouses into one distribution center in Orlando, Fla.; and a major restructuring of Codesco.

Agribusiness

IU's agribusiness subsidiary, C. Brewer and Company, Limited, had revenues of $241.8 million in 1978, up from $236.0 million in 1977. Operating earnings were $1.6 million, compared with $19.2 million in 1977.

While a number of C. Brewer units improved their year-to-year performance, overall operating results for 1978 were disappointing. The principal

Mauna Loa® macadamia nuts, the world's largest selling brand, are grown and marketed by C. Brewer, which plans to more than double the size of its macadamia orchards over the next five years.

causes were depressed prices that plagued the United States sugar industry for the third consecutive year, and a record United States potato crop that lowered prices, contributing to losses at an Oregon-based potato subsidiary. Sale of the potato operations was completed in mid-January 1979.

The political turmoil in Iran in late 1978 led to a write-off of C. Brewer's investment in an agronomics joint venture there. In Guatemala, an unusually strong windstorm destroyed a major portion of the company's macadamia nut orchard. In Hawaii, a loss was incurred on the closing of an obsolete sugar mill to reduce production costs.

Both revenues and earnings were higher from macadamia nuts, coffee, and insurance activities. Molasses, cardamom spice, and chemical operations were profitable, but below 1977 levels.

C. Brewer expects continued growth in 1979 from specialty food operations, particularly macadamia nuts and spices. Molasses and chemical operations should also have improved results in 1979. The company hopes to increase its profit margins by further reducing costs in sugar production and other operations.

C. Brewer continues to reduce its reliance on sugar by expanding and diversifying in other areas. Already the world's largest producer and marketer of macadamias, it will more than double its orchards during the next five years by adding another 5,000 acres to its present 4,000. A number of new-product pilot projects are also under way, including guava puree and freshwater prawns.

Progress is expected in many of C. Brewer's operations in 1979, but the extent of the overall improvement will be determined by the level of sugar prices during the year.

Other operations

IU's other operations produced revenues of $46.7 million in 1978, up 27% from $36.9 million in 1977. Operating earnings were $13.9 million, more than double the $5.1 million of the preceding year.

The large increase in earnings was caused principally by the sale of an office building in Philadelphia and parcels of undeveloped real estate in New Jersey. In addition, the company's silver mining business in Canada's Northwest Territories—Echo Bay Mines Limited—reported improved results, and TAS Communications Services achieved higher revenues and earnings from its telephone-answering, paging and security alarm businesses in Canada.

Principal Subsidiaries

Markets and Operations	Products and Services
Land Transportation **Ryder Truck Lines,** *Jacksonville, Fla.* *Earl N. Hoekenga, Chairman* *Thomas L. Mainwaring, President* **Helm's Express,** *Irwin, Pa.* *W. C. Bender, President* **Byrns Motor Express,** *East Syracuse, N.Y.* *L. E. Johnson, President* **Pacific Intermountain Express,** *Walnut Creek, Calif.* *W. Doyle Beatenbough, President*	IU's trucking companies are among the largest and most efficient motor carriers in the United States, serving nearly every major city through 630 terminals. Ryder and its autonomous Helm's and Byrns divisions serve 34 states in the eastern, central and southwestern United States; P-I-E operates from the East Coast to and along the West Coast in 45 states.
Ocean Shipping **Gotaas-Larsen Shipping Corp.,** *New York and Oslo* *Kenneth A. B. Trippe, President*	Gotaas-Larsen transports liquefied natural gas (LNG), crude and refined petroleum, and chemicals; operates drilling rigs in the North Sea and cruise ships in the Caribbean; and offers maritime engineering, administrative and management consulting services.
Utility Services **Canadian Utilities Limited,** *Edmonton, Alberta* *John E. Maybin, Chairman* *Egerton W. King, President* **General Waterworks Corp.,** *Philadelphia, Pa.* *Allen E. Rosenberg, President*	Canadian Utilities, a 60%-owned subsidiary, supplies electricity to 386 communities and natural gas to 260 communities, mostly in the province of Alberta. General Waterworks, wholly owned by IU, provides water service to more than 260,000 United States customers in 14 states.
Industrial Products and Services **Southwest Fabricating & Welding Co.,** *Houston, Texas* *Bill J. Goodwin, President* **Hills-McCanna Co.,** *Carpentersville, Ill.* *Marvin Altman, President* **Ledeen Flow Control Systems, Inc.,** *Sun Valley, Calif.* *Howard L. Ledeen, Vice President and General Manager* **International Mill Service,** *Philadelphia, Pa.* *Jack Bayer, President* **IU Conversion Systems, Inc.,** *Philadelphia, Pa.* *B. Lawrence Seabrook, Jr., President* **G. & W. H. Corson, Inc.,** *Plymouth Meeting, Pa.* *Augustus D. Lagomarsino, President*	IU's energy-related manufacturing companies make valves, piping, flow control systems, pressure vessels and related components for the power, petroleum, chemical, gas processing and other industries. IU's industrial services companies process slag and reclaim scrap for steel mills in 16 countries; market a service which converts pollutants from coal-burning power plants and other industrial wastes into stable materials for landfill and other uses; and quarry stone and manufacture lime and related materials for metallurgical and construction markets, pollution control and other applications.
Distribution Services **Unijax, Inc.,** *Jacksonville, Fla.* *Walter L. Moore, President* **Biggers Brothers,** *Charlotte, N.C.* *Howard Biggers, Jr., President* **Codesco Inc.,** *Philadelphia, Pa.* *Richard V. Ritchie, President* **Electric Supply Corp.,** *Melrose Park, Ill.* *J. Thomas O'Connor, President* **The Gage Co.,** *Pittsburgh, Pa.* *James E. Montgomery, President* **Taylor Engineering Corp.,** *Detroit, Mich.* *Robert W. Kennedy, President*	IU's major distribution subsidiary, Unijax, supplies paper and related products, disposable items and janitorial supplies to printers and publishers, industrial and commercial customers in 27 states. Other subsidiaries distribute frozen and dry food products to motels, restaurants, fast-food operations, schools, hospitals and others in five Southeastern states; mill supplies, piping and electrical supplies to industrial firms and contractors in six Midwest and Mid-Atlantic states; and dental supplies, equipment and laboratory services to dentists, hospitals, dental laboratories and health care institutions in 26 states.
Agribusiness Products and Services **C. Brewer and Co., Limited,** *Honolulu, Hawaii* *John W. A. Buyers, President*	C. Brewer is a major producer of raw sugar and the world's leading producer and marketer of macadamia nuts and cardamom spice. It also grows other spices, rice, coffee and prawns; markets molasses, chemicals and fertilizers; and provides agronomics consulting and project management services worldwide.
Other **Echo Bay Mines Limited,** *Edmonton, Alberta* *John Zigarlick, Jr., President* **IU Land Development Corp.,** *Philadelphia, Pa.* *Philip S. Cottone, President* **TAS Communications Services,** *Toronto, Ontario* *Robert V. Harwood, President*	IU's other markets include silver mining; telephone answering and paging services for industry, business and individuals; real estate and land development activities; and oil and gas exploration and production in the United States, Canada and the North Sea.

Financial position

Total assets increased to $2,793.5 million in 1978 from $2,704.0 million in 1977. Working capital at year-end 1978 was $90.0 million, compared with $140.1 million at year-end 1977. Net property, plant and equipment rose to $1,660.0 million from $1,591.2 million.

Minority interest increased to $348.0 million at year-end 1978 from $265.5 million at year-end 1977, principally as a result of a preferred equity financing by a Canadian subsidiary. The increase in IU's ownership in C. Brewer and Co. more than offset the decrease in IU's ownership in Canadian Utilities Limited.

Total debt was reduced by $150.4 million to $1,087.8 million during the year, down from $1,238.2 million at year-end 1977. Shareholders' equity grew to $666.9 million from $655.1 million during the year.

Financings

IU and its subsidiaries closed approximately $375 million of new financing in 1978. Financings completed during the year involved public offerings in Canada, short- and medium-term bank credits and term loans in both the United States and European markets, ship mortgage financing, and institutional and private placements in the United States and Canada.

Included in these financings was an institutional private placement of preferred stock in the amount of $100 million by a finance subsidiary. This is the largest single equity financing that IU has ever done. The new security has an average life of 10 years and pays a floating rate dividend. The proceeds from this offering have been used principally to retire debt and improve liquidity.

Available corporate credit capacity was expanded during the year through a $91 million, eight-year, revolving credit and term loan executed by one of the corporate finance companies, substantially replacing its short-term credit facilities. Additionally, a Eurodollar revolving credit was extended to an eight-year revolving credit and term loan and was increased from $30 million to $64 million. These facilities remain principally unutilized, offering significant credit capacity in the event that the company chooses to use it. At year-end 1978, unused credit facilities of the consolidated group totaled more than $300 million.

Canadian Utilities completed a $20 million common stock offering and a $20 million preferred stock offering by a subsidiary during the year. Both transactions were from Canadian sources in Canadian dollars.

Other principal financings during the year included $18 million in ship mortgage financing on the cruise ship "Song of Norway", in which Gotaas-Larsen has a one-third interest, and a $14 million credit facility and term loan for one of the corporation's manufacturing subsidiaries. Short- and medium-term bank credits were obtained for various other operating companies.

Capital expenditures

Capital expenditures totaled $248.6 million in 1978, down 19% from $306.7 million in 1977. For 1979, the company plans capital expenditures of $343.4 million, a 38% increase from 1978. As in 1978, planned expenditures for 1979 are principally for utility services and land transportation.

Retained cash flow and new financing at the operating company level are the principal sources of financing for all of IU's capital expenditures.

Capital Expenditures In millions	**Actual 1977**	**Actual 1978**	**Planned 1979**
Utility services:			
Electric	$ 41.3	$ 42.1	$110.2
Gas	49.6	52.1	54.2
Water	22.3	27.2	24.9
	113.2	121.4	189.3
Land transportation	52.8	59.0	73.0
Ocean shipping	106.2	24.8	15.7
Industrial products and services	22.0	25.6	37.1
Distribution services	4.7	5.3	6.1
Agribusiness products and services	6.7	9.7	19.0
Other	1.1	2.8	3.2
Total capital expenditures	$306.7	$248.6	$343.4

Foreign currency adjustments

Total consolidated foreign currency adjustments resulted in a gain of $11.0 million in 1978, compared with a gain of $14.4 million in 1977 and a loss of $1.4 million in 1976. These adjustments were primarily from the translation of the foreign currency long-term debt of subsidiaries, principally Canadian Utilities, at year-end exchange rates, as required by Financial Accounting Standard No. 8. The exchange rate for the Canadian dollar was $.845 at year-end 1978, $.915 at year-end 1977, and $.990 at year-end 1976. In addition, foreign currency adjustments with respect to long-term debt and commitments of other subsidiaries would have been significant as a result of the weakening of the United States dollar against other major currencies, in particular the Japanese yen and German deutsche mark, if these obligations had not been fully hedged in the forward foreign exchange markets.

In the past three years, foreign currency adjustments have related principally to fluctuations in the Canadian-to-United States currency exchange rates, although the cost of hedging the company's ocean shipping foreign currency exposure is likely to have an increasing effect on currency adjustments in 1979.

Foreign Currency Adjustments*
Effect Per Share

1978			1977	
Quarter	Year to date		Quarter	Year to date
$.13	$.13	First	$.16	$.16
(.05)	.08	Second	(.01)	.15
.16	.24	Third	.08	.23
(.05)	.20	Fourth	.06	.29

*After tax and minority interest

Ten-Year Financial Summary

In millions, except per share data

Operations summary	Revenues and other income
	Cost of sales, other costs and expenses
	Earnings before interest, foreign currency adjustments and taxes
	Interest and debt expense
	Foreign currency adjustments
	Income taxes
	Minority interest
	Earnings from operations[2]
	Net earnings
Earnings per share	Primary:
	Earnings from operations[2]
	Net earnings
	Assuming full dilution:
	Earnings from operations[2]
	Net earnings
Other per share data	Dividends per common share
	Shareholders' equity[3]
	Year-end closing price of common stock[4]
Financial position	Total assets
	Total debt
	Minority interest in subsidiaries
	Shareholders' equity
Other statistics	Property, plant and equipment
	Capital expenditures
	Average common and common equivalent shares[4]

[1]Restated for the accounting changes described in Significant Accounting Policies on page 24.
[2]Before the following credits: in 1972, an extraordinary item of $.7, or $.02 per share both primary and assuming full dilution; in 1970, an extraordinary item of $.1, with no effect per share, and a gain on disposition of properties and investments of $.3, or $.01 per share both primary and assuming full dilution; and in 1969, a gain on disposition of properties and investments of $10.9, or $.37 per share primary and $.30 per share assuming full dilution.
[3]Based on common stock and Special Stock, Series A at year-end.
[4]Adjusted for the two-for-one stock split in 1972.

1978	1977[1]	1976[1]	1975[1]	1974[1]	1973[1]	1972[1]	1971[1]	1970[1]	1969[1]
$2,567.3	$2,285.9	$1,965.3	$1,831.3	$1,983.6	$1,546.4	$1,233.2	$1,101.2	$ 984.4	$ 904.4
2,377.8	2,080.1	1,823.5	1,655.3	1,757.6	1,368.7	1,098.0	973.8	877.9	818.5
189.5	205.8	141.8	176.0	226.0	177.7	135.2	127.4	106.5	85.9
104.8	96.1	70.1	60.0	68.5	54.8	40.3	39.4	42.9	34.9
(11.0)	(14.4)	1.4	(7.1)	(2.0)	8.2	1.6	1.8	8.3	—
51.9	38.5	19.6	27.8	53.1	31.8	24.2	26.7	20.0	16.2
31.7	26.7	7.6	14.9	20.6	8.6	8.6	7.8	4.3	7.0
$ 12.1	$ 58.9	$ 43.1	$ 80.4	$ 85.8	$ 74.3	$ 60.5	$ 51.7	$ 31.0	$ 27.8
$ 12.1	$ 58.9	$ 43.1	$ 80.4	$ 85.8	$ 74.3	$ 61.2	$ 51.7	$ 31.4	$ 38.7
$.30	$1.74	$1.27	$2.44	$2.62	$2.32	$1.91	$1.66	$.98	$.94
$.30	$1.74	$1.27	$2.44	$2.62	$2.32	$1.93	$1.66	$.99	$1.31
$.29	$1.65	$1.19	$2.26	$2.38	$2.08	$1.67	$1.42	$.84	$.76
$.29	$1.65	$1.19	$2.26	$2.38	$2.08	$1.69	$1.42	$.85	$1.06
$.925	$.90	$.875	$.85	$.80	$.75	$.725	$.70	$.67	$.65
$18.11	$19.08	$18.17	$17.85	$16.40	$14.52	$13.00	$11.82	$10.70	$10.34
10¼	11¼	11⅞	9¾	8⅝	18½	24⅛	21 9/16	17 15/16	12 3/16
$2,793.5	$2,704.0	$2,444.5	$2,161.5	$2,038.9	$1,727.8	$1,571.7	$1,432.9	$1,343.3	$1,287.8
$1,087.8	$1,238.2	$1,106.2	$927.6	$888.5	$785.1	$738.2	$643.5	$615.5	$578.6
$348.0	$265.5	$228.1	$167.6	$124.6	$109.8	$97.7	$115.0	$118.4	$115.0
$666.9	$655.1	$622.7	$607.4	$555.0	$492.3	$439.7	$404.7	$367.3	$354.7
$2,221.1	$2,110.9	$1,912.6	$1,763.1	$1,645.5	$1,472.5	$1,307.7	$1,174.7	$1,095.3	$1,011.6
$248.6	$306.7	$205.5	$300.1	$252.7	$202.5	$191.4	$136.2	$137.7	$149.6
33.2	33.0	32.8	32.3	32.1	31.2	30.6	29.4	28.6	26.3

Sources of Revenues and Earnings

In thousands, except per share data

	1978	
	Revenues	Operating Earnings
Contributions by major market:		
Utility services:		
Electric	$ 101,518	$ 38,982
Gas	386,456	33,279
Water	64,670	20,982
	552,644	93,243
Land transportation	798,002	59,497
Ocean shipping	112,411	(7,189)
Industrial products and services	242,257	31,180
Distribution services	573,451	9,592
Agribusiness products and services	241,781	1,554
Other	46,770	13,958
Revenues	$2,567,316	
Operating earnings		201,835
Corporate expenses		(12,286)
Interest and debt expense		(104,771)
Foreign currency adjustments		10,972
Income taxes		(51,945)
Minority interest		(31,745)
Net earnings		$ 12,060
Primary earnings per share		$.30

*Restated for the accounting changes described in Significant Accounting Policies on page 24.

1977*		1976*		1975*		1974*	
Revenues	Operating Earnings	Revenues	Operating Earnings	Revenues	Operating Earnings	Revenues	Operating Earnings
$ 88,484	$ 34,145	$ 79,441	$ 32,294	$ 57,224	$ 22,354	$ 47,587	$ 16,668
299,606	26,375	222,413	27,544	143,051	28,023	94,473	19,001
60,792	17,794	55,744	16,185	48,949	14,105	45,416	13,743
448,882	78,314	357,598	76,023	249,224	64,482	187,476	49,412
637,652	44,702	484,340	31,394	383,666	18,981	377,659	16,936
158,067	34,399	143,556	18,351	142,113	12,003	205,419	49,464
224,118	31,377	177,068	20,564	222,512	24,249	267,785	20,211
544,269	3,509	510,835	4,297	490,181	19,810	605,873	21,819
235,974	19,189	254,212	(9,055)	295,868	20,039	302,381	63,910
36,938	5,083	37,657	8,988	47,735	24,334	37,027	12,675
$2,285,900		$1,965,266		$1,831,299		$1,983,620	
	216,573		150,562		183,898		234,427
	(10,810)		(8,779)		(7,957)		(8,357)
	(96,108)		(70,087)		(60,054)		(68,493)
	14,387		(1,443)		7,128		2,024
	(38,521)		(19,552)		(27,752)		(53,136)
	(26,645)		(7,634)		(14,873)		(20,627)
	$ 58,876		$ 43,067		$ 80,390		$ 85,838
	$1.74		$1.27		$2.44		$2.62

Management's Discussion and Analysis

In millions

This summary should be read in conjunction with the detailed information presented in the discussions of operations on pages 1-14, the financial data on pages 15-19, and the Financial Statements and Notes on pages 21-33.

	Increase (decrease) in 1978 over 1977		Increase (decrease) in 1977 over 1976		Principal causes
	Amount	Percent	Amount	Percent	
Revenues and other income	$281.4	12%	$320.6	16%	Most of the increases in both years came from aggresive expansion programs in the land transportation group and higher volume and rate increases in the utilities group. Other factors include market penetration and higher prices in the institutional food and paper product distribution units, and increased demand for metal recovery and pollution control services. In 1978, revenue gains in ocean shipping were offset by a cancellation charge on a liquefied natural gas carrier and a provision for sale of an oil tanker. An office building and a land tract were sold in 1978 at a gain. Three unprofitable industrial distribution units were sold in 1977.
Costs and expenses	$297.7	14%	$256.6	14%	For both years, the largest increases resulted from higher volume and operating costs in the land transportation and utilities groups. Expenses of the industrial services companies were proportional to sales increases, except that IU Conversion Systems was profitable for the first time in 1977 and the industrial products group's margins were affected by strikes in 1978. Declines in ocean shipping operating expenses reflected fleet reductions and vessel layups; expenses of ships delivered in 1977 and 1976 partly offset the decline. Higher margins of the institutional food distribution unit offset lower margins from dental distribution. Agribusiness was affected by a sugar mill closing, wind damage at a macadamia nut orchard, higher cost of purchased molasses, and higher agricultural production costs. Agribusiness expenses in 1977 reflected divestment of several operating units.
Interest and debt expense	$8.7	9%	$26.0	37%	The increases in both years were caused primarily by borrowings associated with additions to the ocean shipping fleet. Interest rates also rose during both periods.
Foreign currency adjustments	$(3.4)	(24%)	$15.8	—	In both years, gains from foreign currency adjustments stemmed from less rapid year-to-year declines in the Canadian-to-United States dollar exchange rate and a continued weakening of the United States dollar against other major currencies.
Income taxes	$13.4	35%	$18.9	96%	The increase in 1978 over 1977 was a result primarily of improved profitability in the utility and land transportation groups. The increase in 1977 over 1976 was largely due to the one-year return to profitability of the agribusiness group because of federal sugar support payments.
Minority interest	$5.0	19%	$19.1	251%	The 1978 increase resulted from higher earnings in United States dollars from utility operations in Canada, along with dividend requirements on new preferred issues by subsidiaries. The 1977 increase reflects the reported earnings of the agribusiness subsidiary and higher earnings in United States dollars of utility operations in Canada.

Financial Statements

IU International Corporation and Subsidiaries

Consolidated Statements of Earnings

In thousands, except per share data

For the years ended December 31,	1978	1977*
Revenues and other income	**$2,567,316**	$2,285,900
Costs and expenses:		
Cost of products sold, other operating costs and expenses, excluding depreciation and amortization	**1,974,937**	1,707,421
Selling, general and administrative expenses, excluding depreciation and amortization	**293,317**	271,910
Depreciation and amortization	**109,513**	100,806
Interest and debt expense	**104,771**	96,108
Foreign currency adjustments	**(10,972)**	(14,387)
Income taxes	**51,945**	38,521
Minority interest	**31,745**	26,645
	2,555,256	2,227,024
Net earnings	**$ 12,060**	$ 58,876
Earnings per share:		
Primary	**$.30**	$1.74
Assuming full dilution	**$.29**	$1.65

Consolidated Statements of Additional Paid-In Capital

In thousands

	1978	1977*
Amount at beginning of year	**$ 134,272**	$ 128,968
Add (deduct):		
Capital in excess of par or stated value of shares issued upon:		
Conversion of Special Stock, Series A into common	**3,573**	2,924
Conversion of preferred stock into common	**614**	785
Exercise of employee stock options	**12**	112
Other adjustments, principally relating to subsidiaries	**(1,031)**	1,483
Amount at end of year	**$ 137,440**	$ 134,272

Consolidated Statements of Retained Earnings

In thousands

	1978	1977*
Amount at beginning of year, as previously reported	**$ 465,982**	$ 435,036
Adjustments for restatements of prior years	**1,034**	1,399
Amount at beginning of year, as restated	**467,016**	436,435
Net earnings	**12,060**	58,876
	479,076	495,311
Deduct (add):		
Dividends:		
Preferred	**1,973**	1,268
Common (per share: 1978–$0.925; 1977–$0.90)	**28,522**	27,069
Treasury stock transactions	**113**	(42)
	30,608	28,295
Amount at end of year	**$ 448,468**	$ 467,016

*Restated for the accounting changes described in Significant Accounting Policies on page 24.

See accompanying Notes to Financial Statements.

Consolidated Balance Sheets
In thousands

December 31,	1978	1977*
Assets		
Current assets:		
Cash, including certificates of deposit and commercial paper (1978-$33,955; 1977-$32,142)	$ 93,642	$ 90,389
Accounts receivable, less allowance (1978-$6,889; 1977-$9,651)	383,843	327,940
Inventories	158,468	161,150
Prepaid expenses and other current assets	32,299	33,792
Total current assets	668,252	613,271
Net investment in direct financing leases	263,343	257,065
Long-term receivables, restricted cash deposits and investments	118,919	157,535
Property, plant and equipment	2,221,060	2,110,897
Less accumulated depreciation and amortization	561,024	519,733
Net property, plant and equipment	1,660,036	1,591,164
Deferred charges, less amortization	30,798	29,593
Intangibles, net, and other assets	52,126	55,385
Total assets	$2,793,474	$2,704,013
Liabilities and shareholders' equity		
Current liabilities:		
Notes payable	$ 36,697	$ 26,500
Accounts payable and accrued liabilities	395,182	303,717
Income taxes	39,505	23,964
Long-term debt—current maturities	106,894	119,008
Total current liabilities	578,279	473,189
Long-term debt, excluding current maturities	944,214	1,092,666
Other liabilities	109,230	92,888
Deferred income taxes	26,341	25,420
Contributions in aid of utility construction	120,526	99,255
Minority interest in subsidiaries	347,990	265,460
Shareholders' equity:		
Series preferred stock	58,910	23,768
Series preference stock	17,290	21,707
Common stock	39,658	38,719
Additional paid-in capital	137,440	134,272
Retained earnings	448,468	467,016
	701,766	685,482
Less shares in treasury, at cost	34,871	30,347
Total shareholders' equity	666,895	655,135
Total liabilities and shareholders' equity	$2,793,474	$2,704,013

*Restated for the accounting changes described in Significant Accounting Policies on page 24.

See accompanying Notes to Financial Statements.

Consolidated Statements of Changes in Financial Position
In thousands

For the years ended December 31,	1978	1977*
Sources of funds:		
Net earnings	**$ 12,060**	$ 58,876
Add net charges not requiring current funds, principally depreciation, amortization and minority interest	**166,640**	116,480
Provided from operations	**178,700**	175,356
Disposition of property, plant and equipment	**48,375**	61,957
Disposition of other noncurrent assets	**26,374**	17,013
Decrease in net investment in direct financing leases	**4,514**	9,252
Issuance of long-term debt	**105,212**	339,930
Increase in other liabilities	**22,607**	17,071
Contributions in aid of utility construction	**21,022**	15,612
Issuance of capital stock, including treasury stock	**775**	1,030
Issuance of preferred stock to acquire minority ownership in a subsidiary	**35,789**	—
Issuance of capital stock by subsidiaries	**134,200**	26,068
Total sources	**577,568**	663,289
Uses of funds:		
Purchase of property, plant and equipment	**248,630**	306,694
Acquisition of net investment in direct financing leases	**10,792**	90,397
Acquisition of other noncurrent assets	**24,862**	42,710
Reduction of long-term debt	**257,335**	216,054
Reduction of other liabilities	**13,194**	3,160
Purchase of minority ownership in a subsidiary	**36,678**	—
Redemption and conversion of preferred stock	**708**	904
Dividends on preferred and common stock	**30,495**	28,337
Other	**4,982**	(495)
Total uses	**627,676**	687,761
Decrease in working capital	**$(50,108)**	(24,472)
Changes in working capital:		
Cash	**$ 3,253**	$(20,703)
Accounts receivable, less allowance	**55,903**	52,977
Inventories	**(2,682)**	(16,302)
Prepaid expenses and other current assets	**(1,493)**	6,015
Total	**54,981**	21,987
Notes payable	**10,197**	(21,237)
Accounts payable and accrued liabilities	**91,465**	22,516
Income taxes	**15,541**	15,810
Long-term debt—current maturities	**(12,114)**	29,370
Total	**105,089**	46,459
Decrease in working capital	**$(50,108)**	$(24,472)

*Restated for the accounting changes described in Significant Accounting Policies on page 24.

See accompanying Notes to Financial Statements.

Significant Accounting Policies

Principles of consolidation

The consolidated financial statements include the accounts of the Corporation and substantially all of its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. Investments in unconsolidated majority-owned subsidiaries and investments in companies and joint ventures owned 20% to 50% are accounted for on the equity basis, and the Corporation's equity in the earnings of such companies is included in consolidated earnings.

The 1977 financial statements have been restated to reflect the retroactive application of Financial Accounting Standard No. 13, "Accounting for Leases," and the equity method of accounting for an interest in an affiliate. The effect of these changes on revenues, net earnings and earnings per share was not material.

Revenue recognition

Ocean shipping revenue is recognized ratably over the lives of the charter agreements.

Sugar produced in Hawaii is sold to a non-profit marketing cooperative in which the agribusiness subsidiary has an approximate 23% interest. Revenues recognized are based on the current average cost per ton or estimated market value per ton, if lower. Under the equity method of accounting for the investment in the cooperative, any estimated profit on sugar is deferred until sold by the cooperative.

Inventories

Inventories generally are stated at the lower of cost or market. Due to diversified operations, several bases of determining cost are used.

In accordance with industry practice in Hawaii, the costs of growing Hawaiian sugarcane are charged against earnings as incurred.

Property, plant and equipment

Property, plant and equipment are recorded at cost. Certain overhead costs incurred during construction are added to the cost of utility plant and ocean vessels. Depreciation is provided principally on the straight-line basis, except for certain ocean shipping subsidiaries which use the declining-balance method, over the estimated useful lives of the related assets. Upon sale or retirement of non-utility properties, costs and related depreciation are eliminated and gains or losses are recorded. Upon sale or retirement of depreciable utility properties, costs are transferred to accumulated depreciation and no gain or loss is recognized.

Certain of the Corporation's non-utility subsidiaries have established policies of capitalizing interest costs, at approximate current borrowing rates, incurred in connection with construction or development of fixed assets, mainly ocean vessels, in order to distribute such costs over the revenue-producing lives of the assets.

Intangibles

Intangibles consist of: (a) trucking subsidiaries' operating rights; (b) net excess of cost of investments in subsidiaries over underlying net assets; and (c) other intangibles.

Intangibles having a limited life are amortized over their estimated useful lives. The excess of the cost of investments in subsidiaries over net assets of companies acquired is being amortized over periods from 10 to 40 years, except that portion relating to companies acquired before October 31, 1970, as long as there is no present indication that such excess has a determinable life or existence.

Income taxes

Provision is made for deferred income taxes and future income tax benefits applicable to timing differences between financial statement and taxable income, except that certain utility subsidiaries claim depreciation and certain other expenses for income tax purposes in excess of the amounts recorded in the accounts without providing for the related income tax deferral. In setting rates, these utilities recover only income taxes payable currently.

Certain subsidiaries operate in countries where their earnings are substantially free of taxation or are taxed at rates effectively lower than in the United States. Income taxes have been provided on that portion of the earnings of such subsidiaries considered not to be continuously reinvested outside the United States.

Investment tax credits are accounted for by the flow-through method, except that utility subsidiaries allocate the credits over the depreciable lives of the related assets.

Earnings per share

Primary earnings per share, computed after deducting the dividend requirement on preferred stock, are based on the average number of shares of both common and Special Stock, Series A outstanding each year and the dilutive

effect of stock option and stock purchase plans and warrants. The Special Stock, Series A has been included using 3.0790 and 2.9604 common shares of the Corporation for 1978 and 1977, respectively, the applicable conversion rates.

Earnings per share assuming full dilution reflect, in addition to the primary computation, the dilutive effect of (a) the conversion of convertible preferred stock and convertible bonds after the elimination of the dividend requirements on such convertible preferred stock and the interest, net of income taxes, applicable to the convertible bonds, and (b) the conversion of Special Stock, Series A at the rates in effect 10 years after each period.

Acquisitions and Dispositions

On August 14, 1978, the Corporation acquired the 46% minority ownership in C. Brewer and Company, Limited (Brewer) in exchange for 2,136,638 shares of the Corporation's $1.36 convertible preferred stock valued at $16.75 per share (see Commitments and Contingencies on page 32). The acquisition was accounted for as a purchase. The excess of the value assigned to the net assets acquired over the value of the stock issued has been allocated proportionately to noncurrent assets. The results of operations of Brewer are included in consolidated net earnings based upon the 100% ownership from the merger date. If this acquisition had occurred on January 1, 1977, the Corporation's net earnings and earnings per share would have been approximately as follows:

	1978	1977
Net earnings (in thousands)	$13,732	$62,063
Earnings per share	$0.30	$1.76

In addition, during 1978 and 1977, the Corporation acquired several smaller companies in purchase transactions for notes and cash amounting to an aggregate consideration of $5,002,000 and $765,000, respectively. The operations of these companies are not significant.

During the two years ended December 31, 1978, the Corporation disposed of certain foreign freight-forwarding companies, a potato products company, the fabrication division of a distribution company, three industrial distribution companies, two hotels, four shipping companies and certain other small companies. The contribution to revenues and net earnings, excluding gains and losses on disposition, of such companies for the years ended December 31, 1978 and 1977 was as follows:

In thousands	1978	1977
Revenues	$22,985	$95,565
Net loss	(4,966)	(6,462)

Geographic Information

A summary of significant items with respect to operations in major geographic areas is as follows:

In thousands	Revenues	Net earnings	Working capital	Total assets
1978:				
Canada	$ 522,714	$32,710	$ (17,715)	$ 809,390
International (ocean shipping)	112,411	(53,756)	(72,259)	783,704
Other non-United States	126,859	1,374	18,667	108,966
Total non-United States	761,984	(19,672)	(71,307)	1,702,060
United States	1,805,332	31,732	161,281	1,091,414
Total	$2,567,316	$12,060	$ 89,974	$2,793,474
1977:				
Canada	$ 420,556	$29,287	$ 1,565	$ 727,933
International (ocean shipping)	158,067	(1,585)	(24,057)	823,636
Other non-United States	116,404	4,714	12,542	97,833
Total non-United States	695,027	32,416	(9,950)	1,649,402
United States	1,590,873	26,460	150,032	1,054,611
Total	$2,285,900	$58,876	$140,082	$2,704,013

Operations in Canada relate principally to electric and gas utility services. On its major routes, the ocean shipping fleet transports refined and crude oil products and chemicals from the Middle East, Nigeria and Venezuela to Great Britain, North America, Europe and Japan, and LNG from Abu Dhabi to Japan. Its offshore drilling rigs are employed in the North Sea. The cruise ships operate principally in the Caribbean area. Corporate assets are located within the United States.

Income Presentation

Included in revenues and other income are net product sales of $1,038,725,000 and $976,636,000 for 1978 and 1977, respectively.

Included in other income are the following significant items:

In thousands	1978	1977
Interest and dividends from securities	$ 9,903	$7,802
Gain (loss) on sale or disposition of ships	(15,469)	5,610
Loss on cancellation of construction contract	(26,862)	—
Gain (loss) on disposition of investments and certain other assets	9,825	(3,522)
Gain on sale of unutilized land	810	3,793
Operations of divested subsidiaries	(4,082)	(884)

During 1978 and 1977, the ocean shipping subsidiary sold or disposed of several vessels at a net gain (loss) of $(15,469,000) and $5,610,000, respectively. Included in the net loss for 1978 is approximately $18,100,000 provided in December in connection with the decision to sell a large oil tanker.

Also in December 1978, the ocean shipping subsidiary provided for a net loss of $26,862,000 as a result of an agreement, subject to approval by the Japanese government, to cancel a construction contract for a liquefied natural gas carrier.

During 1978, the Corporation sold several subsidiaries and certain other assets at a gain of $9,825,000 after application of reserves of $4,338,000 provided in prior years. Income taxes of $213,000 have been provided with respect to these dispositions.

During 1977, the Corporation sold or liquidated several subsidiaries and certain other assets at a loss of $3,522,000 after application of reserves of $7,157,000 provided in prior years. Income tax benefits of $2,634,000 have been recognized with respect to these dispositions.

In connection with the gain on sale of unutilized land by the agribusiness subsidiary, income taxes of $414,000 and $1,955,000 have been provided in 1978 and 1977, respectively.

The pretax operating results of divested subsidiaries have been included in other income from the respective dates the Corporation committed itself to dispose of the companies.

In addition, in December 1978, the ocean shipping subsidiary provided $4,804,000 for the remaining obligation on a charter-in agreement extending through 1980 for a vessel presently in layup. The agribusiness subsidiary wrote off deferred charges applicable to orchards damaged by severe weather and the undepreciated cost of a closed sugar mill amounting to $1,916,000. All of these charges have been included in other operating costs; tax benefits of $1,435,000 were recognized with respect to these items.

Inventories

The summary of inventories at December 31, 1978 and 1977 is shown in the following table:

In thousands	1978	1977
Finished products	$ 63,660	$ 64,891
Work in process	6,303	12,589
Raw materials and supplies	40,114	40,703
Merchandise and commodities	47,232	39,066
Other	1,159	3,901
	$158,468	$161,150

Certain items included in merchandise and commodities are valued on the last-in, first-out (LIFO) basis, which is approximately $5,969,000 and $5,117,000 at December 31, 1978 and 1977, respectively, less than the cost of such inventories valued on the first-in, first-out (FIFO) basis.

The December 31, 1978 book basis of LIFO inventories exceeded the tax basis by $1,951,000. The difference resulted from the application of purchase accounting to the acquisition of the minority interest in Brewer. Income for federal tax purposes for 1978 is higher by $426,000 because of this difference in basis.

Long-Term Receivables, Restricted Cash Deposits and Investments

The total carrying values of long-term receivables, restricted cash deposits and investments at December 31, 1978 and 1977 are shown in the table to the right.

Dividends received from unconsolidated subsidiaries, joint ventures and cooperatives were $4,243,000 in 1978 and $4,561,000 in 1977.

In thousands	1978	1977
Long-term receivables	$ 21,104	$ 35,913
Restricted cash deposits	23,776	26,521
Land held for sale or development	11,162	20,355
Unconsolidated subsidiaries and affiliates	18,597	17,778
Joint ventures, principally partnerships in vessels	28,669	34,442
Cooperatives	13,367	22,322
Other investments	3,996	4,067
Provision for loss	(1,752)	(3,863)
	$118,919	$157,535

Property, Plant and Equipment

A summary of property, plant and equipment at December 31, 1978 and 1977 is shown in the table to the right.

A tanker for which a preliminary agreement of sale has been reached and a liquefied natural gas carrier were in layup at December 31, 1978. The total carrying value of both vessels at December 31, 1978 was approximately $150,000,000.

Interest and other overhead costs of $17,557,000 in 1978 and $15,070,000 in 1977, relating principally to the construction of utility plant and vessels, were capitalized.

In thousands	1978	1977
Utility services	$1,118,969	$1,012,761
Land transportation	283,641	243,758
Industrial products and services	145,081	126,709
Ocean shipping	478,349	489,968
Distribution services	43,518	42,738
Agribusiness products and services	127,282	158,460
Other	24,220	36,503
	2,221,060	2,110,897
Less accumulated depreciation and amortization	561,024	519,733
	$1,660,036	$1,591,164

Debt

Short-term notes payable at December 31, 1978 and December 31, 1977, of which $1,317,000 and $1,050,000, respectively, are secured, have an average interest rate of 11% and 9%, respectively, and represent borrowings by subsidiaries under lines of credit. During 1978 and 1977, the maximum month-end borrowings under short-term credit arrangements amounted to $38,000,000 and $69,000,000, respectively; the average month-end borrowings under these agreements were $30,000,000 and $44,000,000, respectively, and had weighted average interest rates of 11% and 9%, respectively. At December 31, 1978, unused short-term credit facilities amounted to $68,000,000 and unused long-term credit facilities amounted to $261,000,000, respectively.

Long-term debt at December 31, 1978 and 1977 payable by subsidiaries is summarized in the following table. Interest rates on approximately $271,000,000 of long-term debt outstanding at December 31, 1978 are based on United States prime, Eurodollar, or other fluctuating interest rates.

In thousands	1978	1977
First mortgage bonds:		
Due 1978 to 1996; 3½% to 9¾% (weighted average interest rate 6.5% in 1978, 6.4% in 1977)	$ 101,933	$ 112,743
Other:		
Secured:		
Due 1978 to 2002; 2% to 21% (weighted average interest rate 10.2% in 1978, 8.6% in 1977)	571,248	596,370
Unsecured:		
Due 1978 to 2002; 5¼% to 18% (weighted average interest rate 10.0% in 1978, 9.0% in 1977)	377,927	502,561
	1,051,108	1,211,674
Less current maturities	106,894	119,008
	$ 944,214	$1,092,666

The mortgage bonds and secured debt are subject to various indentures and agreements requiring, among other things, either the mortgaging of properties, the pledging of investments in subsidiaries, or in certain instances a combination of both. At December 31, 1978, investments in direct financing leases and property, plant and equipment with a total carrying value of $1,208,000,000 secured such debt. Sinking fund requirements and installments of long-term debt maturing in the years 1980, 1981, 1982 and 1983 amount to approximately $142,488,000, $119,876,000, $115,659,000 and $112,081,000, respectively, after deducting bonds which have been repurchased and excluding requirements which may be satisfied by certification of property additions.

The Corporation maintains cash balances at certain banks related, in part, to the outstanding balance of certain bank loans and, in part, to anticipation of future credit negotiations. At December 31, 1978, the bank-collected balance under such arrangements, as reported by the respective banks, was approximately $30,000,000 and the related book balance was approximately $19,000,000. The aggregate average bank-collected balance maintained during 1978, as reported by the respective banks, was approximately $33,000,000 and the related average month-end book balance was approximately $30,000,000. These funds are not subject to withdrawal restrictions.

The bond indentures and note agreements executed by the Corporation and certain subsidiaries require the maintenance of specified ratios of consolidated net worth and total capitalization, as therein defined, and limit the payment of dividends on capital stock of the Corporation. Under the most restrictive covenant, which specifies capitalization requirements, approximately $42,000,000 of the consolidated retained earnings at December 31, 1978 was free from restriction.

Pension Plans

The Corporation and certain of its subsidiaries have insured or trusteed pension plans, some of which require employee contributions. These plans generally provide for normal retirement at age 65. The unfunded pension liabilities under such plans are amortized over periods not exceeding 40 years. It is the Corporation's general policy to fund pension costs accrued.

At December 31, 1978, based on the latest actuarial valuations, the total unfunded pension liability amounted to approximately $56,334,000 and the unfunded vested liability (net of balance sheet accruals) was estimated to be $13,015,000. Total pension costs charged against earnings during the years ended December 31, 1978 and 1977 were $16,218,000 and $14,938,000, respectively.

Income Taxes

The components of the provision for income taxes for the years ended December 31, 1978 and 1977, are as follows:

In thousands	1978	1977
Current:		
Federal	$19,333	$12,343
State and local	5,352	3,045
Non-United States	29,397	20,726
Investment tax credit	(5,971)	(5,069)
	48,111	31,045
Deferred:		
Federal	2,756	7,403
State and local	62	1,273
Non-United States	1,016	(1,200)
	3,834	7,476
	$51,945	$38,521

The sources of the differences between earnings for financial statement purposes and tax purposes and the tax effects are as follows:

In thousands	1978	1977
Excess of tax over book depreciation	$6,937	$7,937
Foreign tax credits	3,079	(3,079)
Undistributed earnings of foreign subsidiaries	2,000	—
Earnings on long-term construction contracts	1,661	(68)
Recovery of loss on investments and other assets	1,177	3,824
Unrealized foreign currency exchange loss	(6,895)	(1,811)
Provision for self-insurance claims	(1,794)	(255)
Excess of book over tax (tax over book) revenues from sugar sales (included in current liabilities)	(298)	3,713
Other	(2,033)	(2,785)
	$3,834	$7,476

The Corporation's effective tax rates of 81.2% and 39.6% for the years 1978 and 1977, respectively, varied from the United States income tax rate of 48.0% for the reasons shown in the following table.

	1978	1977
Federal income tax rate	48.0%	48.0%
Loss (earnings) from non-United States subsidiaries continuously reinvested outside the United States	32.3	(1.0)
Loss (earnings) of foreign subsidiaries taxed below United States rates, and related dividends	13.8	(1.4)
Accelerated depreciation, depletion and other expenses, principally utility operations	(15.6)	(9.5)
Investment tax credit	(9.3)	(5.2)
Minority interest with no tax effect	23.8	13.1
State and local income taxes, net of federal tax benefit	4.4	2.3
Capital gains rate	(4.9)	(.5)
Foreign currency translation	(11.7)	(9.0)
Other	.4	2.8
Effective tax rate	81.2%	39.6%

At December 31, 1978, the Corporation had not provided income taxes on $158,000,000 of undistributed earnings of non-United States subsidiaries, since such earnings are being continuously reinvested in plant and vessels outside the United States and it is the Corporation's intention to continue this policy.

The Corporation has received notices of tax deficiencies with respect to 1968-1970 (which presently are being contested in Tax Court), and has pending claims for partial refund of tax assessments paid with respect to 1971-1972. The Corporation has also received notices of proposed tax adjustments with respect to 1973-1974 (which presently are being protested with the Internal Revenue Service), some of which could result in substantial tax deficiencies and may impact subsequent years. The more significant items involve current deductibility of certain expenditures which were capitalized in the water utility rate setting process, the current deductibility of a foreign exchange loss, and the taxation of intercompany loans between foreign subsidiaries as dividends to the United States parent corporation. The Corporation does not agree with the notices of tax deficiencies and the proposed adjustments, and believes that it has sound arguments in support of its positions. While the final outcome of these matters is not determinable at this time, management believes the ultimate liability, if any, will not materially affect the financial position of the Corporation.

Capital Stock

The authorized and issued capital stock of the Corporation at December 31, 1978 and 1977 is summarized below:

In thousands, except share data, issued at December 31,	1978		1977	
	Shares	Stated or par value	Shares	Stated or par value
Series preferred stock, without par value:				
Authorized: 4,814,708 shares (reserved for issuance of floating rate preferred stock—1,000,000 shares; for exercise of options—134,200 shares)				
Issued:				
$5.00 series (in treasury at both dates—3,760 shares)	93,302	$9,563	93,302	$ 9,563
$1.25 convertible series (in treasury at both dates—304,532 shares) with aggregate liquidation value at December 31, 1978 of $22,279	891,148	13,505	937,307	14,205
$1.36 convertible series (in treasury at December 31, 1978—276,766 shares) with aggregate liquidation value at December 31, 1978 of $48,200	2,142,203	35,842	—	—
	3,126,653	58,910	1,030,609	23,768
Series preference stock, without par value:				
Authorized: 5,462,946 shares				
Issued: Special Stock, Series A (in treasury at both dates—176,371 shares)	892,985	17,290	1,121,153	21,707
Common stock, par value $1.25 per share:				
Authorized: 60,000,000 shares (reserved for conversion of preferred stock—4,271,341 shares; for conversion of Special Stock, Series A—3,913,239 shares; for conversion of bonds of a subsidiary—155,375 shares; and for stock option and stock purchase plans—2,607,919 shares)				
Issued (in treasury at both dates—738,644 shares)	31,726,086	39,658	30,974,861	38,719

The holders of preferred stock are entitled to cumulative dividends at the respective rates set out in the titles of the various series and have voting rights. The holders of the $5.00 preferred stock, upon liquidation or redemption, are entitled to receive the stated value plus accrued and unpaid dividends. The $1.25 convertible preferred stock is redeemable, at the Corporation's option, at $25 per share. Each share of the $1.25 convertible preferred stock is convertible into 1.6 common shares. The $1.36 convertible preferred stock is redeemable, at the Corporation's option, at $26.25 through August 14, 1979 and at decreasing amounts thereafter. Each share of the $1.36 convertible preferred stock is convertible into 1.25 common shares.

Holders of Special Stock, Series A are not entitled to receive dividends; they have voting rights and on liquidation are entitled to receive $15 per share subject to the liquidation rights of the preferred shareholders. The Special Stock, Series A is convertible into 3.0790 and 2.9604 shares of common stock through December 31, 1979 and 1978, respectively, after which the conversion rates increase annually to a maximum of 4.3822 common shares on January 1, 1988. The stock is redeemable, at the Corporation's option, at $70 per share.

Changes in capital stock during the years ended December 31, 1978 and 1977 are summarized as follows:

	1978			1977		
	Preferred	Special Stock, Series A	Common	Preferred	Special Stock, Series A	Common
Shares issued at beginning of year	1,030,609	1,121,153	30,974,861	1,090,265	1,306,307	30,340,103
Issuance of preferred stock	2,136,638	—	—	—	—	—
Conversion of Special Stock, Series A	—	(228,168)	675,384	—	(185,154)	526,933
Conversion of preferred stock	(46,594)	—	74,391	(59,656)	—	95,442
Exercised under stock option plan	6,000	—	1,450	—	—	12,383
Shares issued at end of year	3,126,653	892,985	31,726,086	1,030,609	1,121,153	30,974,861

At December 31, 1978, 276,766 shares of $1.36 convertible preferred stock were held by Brewer, of which 258,825 are issuable to Brewer's former minority shareholders. Other changes in treasury stock during the years ended December 31, 1978 and 1977 consisted of the expiration of warrants originally attached to bonds issued by a subsidiary and the issuance of 13,131 shares of common stock in settlement of a subsidiary acquisition, respectively.

Bonds of a wholly-owned subsidiary due in 1986 with an outstanding principal amount of $2,486,000 at December 31, 1978 are convertible prior to maturity into common stock of the Corporation at $16 per share.

At December 31, 1978, a wholly-owned subsidiary had outstanding $100,000,000 of preferred stock. The stock has mandatory redemption requirements beginning in 1986 and a floating dividend rate, currently 7.2%. Under certain conditions, the Corporation may substitute similar stock of the Corporation or guaranteed subordinated promissory notes for the subsidiary's securities.

Stock Options

Options to certain officers and employees of the Corporation and its subsidiaries were outstanding at December 31, 1978 and 1977 pursuant to qualified stock option plans, and a nonqualified stock option and stock unit award plan. Options are exercisable in varying amounts over periods from one to 10 years from the date of grant, at prices from 85% to 100% of the fair market value of the stock at the date of grant.

The changes in the outstanding options for common stock during 1978 and 1977 are shown in the table to the right.

	1978	1977
Shares under option at beginning of year	784,008	705,236
Granted	230,000	206,500
Exercised	(1,450)	(12,383)
Converted to stock units	—	(89,600)
Cancelled or expired	(121,546)	(25,745)
Shares under option at end of year	891,012	784,008
Average option price	$12.37	$13.57

At December 31, 1978, there were 448,355 shares of common stock reserved for future grants under the stock option plan.

In addition, options for 134,200 shares of $1.36 convertible preferred stock were outstanding at December 31, 1978 with an average option price of $15.32. These options were assumed by the Corporation upon the acquisition of Brewer. Options covering 6,000 shares were exercised during the year.

Under the nonqualified stock option and stock unit award plan, options which have been elected as stock units entitle the grantee, subject to the provisions of the plan, to a cash distribution rather than common stock of the Corporation. At December 31, 1978, there were 42,800 stock units outstanding. A qualified stock option which is not exercised prior to May 21, 1981 will become a non-qualified option on that date by operation of law.

Under the employee stock purchase plan, 1,268,552 shares of common stock are available for future issuance to eligible employees. During 1978, an offering was made at a purchase price of 85% of the mean market price on September 30, 1980, but not exceeding $9.62. Subscriptions for 1,040,974 shares were outstanding at December 31, 1978.

Operating Segment Information

The revenues and operating earnings information for 1978 and 1977 on pages 18-19, capital expenditures for 1978 and 1977 on page 15, and the description of products and services of each segment on page 14 are an integral part of these statements and should be read in conjunction with this note.

Identifiable assets as of December 31, 1978 and 1977 and depreciation and amortization for the years 1978 and 1977 are presented below by major market segment. Corporate assets are principally cash and investments.

In thousands	Identifiable Assets		Depreciation and Amortization	
	1978	1977	1978	1977
Utility services:				
Electric	$ 377,205	$ 354,185	$ 13,416	$ 11,060
Gas	403,701	347,748	8,868	7,084
Water	264,468	242,335	4,610	4,422
	1,045,374	944,268	26,894	22,566
Land transportation	321,857	266,726	28,018	24,550
Industrial products and services	184,356	155,046	14,438	13,097
Ocean shipping	783,704	823,636	25,724	26,140
Distribution services	180,282	177,237	3,235	3,096
Agribusiness products and services	220,591	263,816	8,072	8,445
Other	36,120	45,253	2,665	2,662
Corporate	21,190	28,031	467	250
Total	$2,793,474	$2,704,013	$109,513	$100,806

Leasing Activities

The ocean shipping subsidiary has chartered out certain vessels under long-term agreements which are accounted for as direct financing leases. A provision of certain charters permits suspension of charter hire under certain conditions. The off-hire periods are added to the end of the charters, and interest is payable on the deferred charter hire receivable. The components of the net investment in direct financing leases at December 31, 1978 and 1977 are shown in the table to the right.

At December 31, 1978, other vessels owned by the ocean shipping subsidiary with a carry-

In thousands	1978	1977
Total minimum charter hire receivable	$960,216	$1,013,729
Less operating costs and related profit	363,180	379,806
Minimum charter hire receivable	597,036	633,923
Estimated residual value	75,406	75,311
Deferred charter hire receivable	10,697	—
Less unearned income	415,380	448,109
Net investment in direct financing leases	267,759	261,125
Less current maturities	4,416	4,060
	$263,343	$ 257,065

ing value of $271,506,000, net of accumulated depreciation of $60,844,000, were on charter or held for charter. Future minimum charter hire receivable under direct financing and operating leases, including amounts representing estimated operating costs and related profit, was approximately:

In thousands	Direct financing leases	Operating leases
1979	$ 53,415	$23,710
1980	53,415	4,230
1981	53,321	163
1982	55,061	—
1983	55,890	—
Thereafter	689,114	—
Total	$960,216	$28,103

The Corporation and its subsidiaries lease certain vessels, facilities and equipment. Total rental expense, including short-term leases and immaterial amounts of contingent rents, for 1978 and 1977 was $151,340,000 and $96,836,000, respectively. Sublease income from these leases, which is included in revenues and other income, was $16,631,000 and $24,781,000, respectively.

The future minimum lease payments under all noncancellable leases, before deducting minimum sublease rentals of $2,119,000 on capital leases and $10,834,000 on operating leases, were approximately:

In thousands	Capital leases	Operating leases
1979	$ 6,288	$25,112
1980	6,053	19,513
1981	5,865	11,323
1982	5,455	7,523
1983	5,092	6,407
Thereafter	54,928	27,717
	83,681	$97,595
Less amount representing interest	36,497	
Present value of net minimum lease payments	$47,184	

Minimum lease payments under capital leases include interest at rates ranging from 2% to 21%; the present value of these lease payments is included in long-term debt. At December 31, 1978 and 1977, assets under capital leases, principally ocean vessels, with a carrying value of $41,007,000 and $43,842,000, respectively, net of accumulated depreciation of $24,317,000 and $22,540,000, respectively, are included in property, plant and equipment.

Commitments and Contingencies

At December 31, 1978, outstanding contractual commitments of certain subsidiaries amounted to approximately $186,600,000 for the construction of vessels (at exchange rates in effect on December 31, 1978); approximately $29,128,000 for the purchase of equipment and operating rights for the trucking companies; and approximately $144,345,000 for the construction of new utility plant. Contractual commitments for vessels have been adjusted to reflect an agreement reached with the shipbuilder to cancel one liquefied natural gas carrier and to defer delivery of the remaining liquefied natural gas carrier on order. This agreement is subject to approval by the Japanese government. Mortgage financing of $149,500,000 has been arranged with respect to a portion of the commitments. Of this total amount, $131,500,000 is available subject to agreement on security. A total of $115,610,000 of the outstanding contractual commitments becomes due for payment in 1979.

In addition, certain subsidiaries are directly liable for their proportionate share of mortgage loans on vessels and rigs in operation in the amount of $25,500,000 at December 31, 1978, and are contingently liable for the other partners' share in the amount of $19,500,000.

Several actions have been commenced alleging violations of law in connection with the merger, effective August 14, 1978, between C. Brewer and Company, Limited and a wholly-owned Hawaii subsidiary of the Corporation. In one of these actions, the First Circuit Court of Hawaii on January 9, 1979 entered an order setting aside the merger. This decision has been appealed to the Supreme Court of Hawaii, and implementation of the lower court's decision has been stayed pending the determination thereof. In addition, holders of 248,726 shares of Brewer stock have brought actions under Hawaii's dissenters' rights statute to have the court determine the fair market value of their shares. While the final outcome of these matters is not determinable at this time, management believes that the ultimate resolution will not materially affect the financial position of the Corporation.

During 1978, an ocean shipping subsidiary was sued in The High Court in London by the time charterer of the subsidiary's liquefied natural gas carrier for various items of damages aggregating approximately $7,000,000, net of insured items. The damages were allegedly suffered by plaintiff owing to the presence of debris in the vessel's discharging lines, which it is alleged was the cause of a suspension of discharge of cargo starting in May 1977. The subsidiary has been advised by its legal counsel that defenses are available to it which are expected to defeat or substantially mitigate the claims.

Quarterly Operating Results (Unaudited)

The following is a summary of the unaudited quarterly operating results for the two years ended December 31, 1978:

In thousands, except per share data	Revenues and other income	Cost of products sold, other operating costs and expenses	Net earnings (loss)	Earnings (loss) per share: Primary	Earnings (loss) per share: Assuming full dilution
For the year 1978:					
First quarter	$ 630,211	$ 466,748	$23,189	$ .69	$ .65
Second quarter	628,586	468,389	14,658	.43	.41
Third quarter	634,286	485,178	15,976	.46	.44
Fourth quarter	674,233	554,622	(41,763)	(1.38)	(1.38)
Full year	$2,567,316	$1,974,937	$12,060	.30	.29
For the year 1977:					
First quarter	$ 554,386	$ 409,587	$21,636	.64	.60
Second quarter	561,459	423,381	10,321	.30	.29
Third quarter	567,502	427,385	13,509	.40	.37
Fourth quarter	602,553	447,068	13,410	.40	.38
Full year	$2,285,900	$1,707,421	$58,876	1.74	1.65

Quarterly earnings per share do not total full year earnings per share because of the antidilutive effect of convertible securities.

Foreign currency adjustments resulted in the gains (losses) shown in the table to the right.

In thousands	1978	1977
First quarter	$ 7,190	$ 8,429
Second quarter	(2,907)	(807)
Third quarter	8,887	3,673
Fourth quarter	(2,198)	3,092
Full year	$10,972	$14,387

Replacement Cost (Unaudited)

In accordance with Securities and Exchange Commission regulations, management has estimated the current replacement cost of certain inventories and productive capacity of the Corporation and its consolidated subsidiaries as of December 31, 1978 and 1977, together with related amounts of cost of sales and depreciation and amortization. Such information is included in the Corporation's Annual Report to the Securities and Exchange Commission on Form 10-K.

The estimated replacement cost of inventories and the related amount of cost of sales do not significantly exceed the related historical dollar amounts.

The estimated replacement cost of certain property, plant and equipment and the related amount of depreciation and amortization significantly exceed the related historical dollar amounts reflecting the cumulative impact of inflation principally on the long-lived assets of the utility subsidiaries.

Although the replacement cost data has, in the Corporation's view, been estimated in a reasonable manner, it is the opinion of management that the data is of limited value because of the subjectivity necessarily involved in making these estimates. The data should not be construed to represent either the Corporation's intent to replace existing assets or, even if such assets were replaced, to represent the actual costs of such future replacements.

PEAT, MARWICK, MITCHELL & CO.
CERTIFIED PUBLIC ACCOUNTANTS
1500 WALNUT STREET
PHILADELPHIA, PA. 19102

The Board of Directors and Shareholders
IU International Corporation
Wilmington, Delaware

We have examined the consolidated balance sheets of IU International Corporation (a Maryland corporation) and subsidiaries as of December 31, 1978 and 1977, and the related consolidated statements of earnings, additional paid-in capital, retained earnings, and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of IU International Corporation and subsidiaries at December 31, 1978 and 1977, and the results of their operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis, after restatement for the change, with which we concur, in the method of accounting for leases in accordance with Statement of Financial Accounting Standards No. 13, "Accounting for Leases," as described in the Significant Accounting Policies note to the financial statements.

Peat, Marwick, Mitchell & Co.

February 28, 1979

Shareholder Data

Shareholders

IU International had 44,466 shareholders at year-end 1978, including 34,762 holders of common stock and 9,704 holders of preferred and preference stock.

On December 31, 1978, there were 30,987,442 shares of IU common stock outstanding; 716,614 shares of Special Stock, Series A outstanding; 586,616 shares of $1.25 Convertible Preferred Stock outstanding; 1,865,437 shares of $1.36 Convertible Preferred Stock outstanding; and 89,542 shares of $5.00 Preferred Stock outstanding.

Common stock registration	Number of holders	Number of shares	% of total
Individuals	32,303	10,838,024	35%
Banks, securities firms and depositary trusts	1,251	17,626,598*	57
Foundations, corporations, unions and pension plans	1,208	2,522,820	8
Total	34,762	30,987,442	100%

*Includes shares held beneficially on behalf of an estimated 10,000 individual shareholders.

During 1978, the trading volume of IU common stock on all exchanges was 9,736,192 shares. Of these, 7,662,840 shares were traded on United States stock exchanges.

In 1977, a total of 10,270,576 shares of IU common stock was traded on all exchanges; 7,787,832 were traded on United States exchanges.

Dividends

Dividend payments are made to IU shareholders on the first business day of March, June, September, and December. Total dividends paid during 1978 were $30.5 million. Owners of common stock were paid $28.5 million, and owners of preferred stock received $2.0 million.

Improved Dividend Reinvestment Plan

As a result of recent improvements in IU's Dividend Reinvestment Plan, common and preferred shareholders may reinvest their quarterly dividends in IU common stock—free of all brokerage and administrative charges beginning with the March 1, 1979 dividend. Shareholders now have the option to reinvest a portion of their dividends and receive the balance in cash. New cash investments of up to $5,000 per quarter also may be made at no additional charge. A brochure describing the program is available from the company's Corporate Affairs Department, 1500 Walnut Street, Philadelphia, Pa. 19102, and from the Dividend Reinvestment Service Offices of Morgan Guaranty Trust Company, P. O. Box 3506, New York, N.Y. 10008.

Stock Exchanges

IU's capital stock is listed for trading (symbol: IU) on these exchanges: New York, Philadelphia, Midwest, Pacific, Toronto, Montreal, Vancouver, London, Amsterdam, Oslo and Tokyo.

Transfer Agents and Registrars

The transfer agents for IU's capital stock are Morgan Guaranty Trust Company of New York; Wilmington Trust Company in Wilmington; Bank of America, N. T. & S. A. in San Francisco; and Montreal Trust Company in Montreal, Toronto, Calgary, Vancouver and Regina. The registrars are Chemical Bank in New York; Wilmington Trust Company in Wilmington; Wells Fargo Bank N.A. in San Francisco; Crown Trust Company in Montreal, Toronto, Calgary and Vancouver; and The Royal Trust Company in Regina.

Investor Services

IU maintains an investor relations office within its Corporate Affairs Department at 1500 Walnut Street, Philadelphia, Pa. 19102. Beneficial shareholders who experience delays in receiving IU financial reports from their brokerage firms are invited to write directly to the Corporate Affairs Department for interim and annual reports.

IU's Annual Report to the Securities and Exchange Commission on Form 10-K and the company's Facts & Figures Manual will be available, on request, from IU's Corporate Affairs Department, 1500 Walnut Street, Philadelphia, Pa. 19102.

Capital Stock Summary

The cash dividends and the high and low prices of the company's stock on the New York Stock Exchange are shown in the table to the right. The Special Stock, Series A is not entitled to cash dividends, but is convertible into common stock at an increasing ratio.

The company's $5.00 Preferred Stock does not trade actively and is not included in the table. During 1978 and 1977, the bid prices were $45 and $55 per share, respectively. Dividends of $1.25 per share were paid in each quarter of 1978 and 1977 to holders of this stock.

	Common Stock			Special Stock, Series A		$1.25 Convertible Preferred Stock			$1.36 Convertible Preferred Stock*		
	Dividend	High	Low	High	Low	Dividend	High	Low	Dividend	High	Low
1978:											
4Q	$.2375	12½	9⅞	35¾	28⅞	$.3125	19¼	15⅞	$.4071	16⅜	13⅜
3Q	.2375	13	11	38	33	.3125	21¼	17⅞	—	17	15¼
2Q	.2250	12¼	10⅞	35⅜	33	.3125	19½	17⅞	—	—	—
1Q	.2250	11⅞	10¾	34½	32	.3125	18½	17¼	—	—	—
1977:											
4Q	.2250	12⅛	10⅞	34	31½	.3125	18½	17¾	—	—	—
3Q	.2250	14⅜	11½	40	32½	.3125	22⅜	18½	—	—	—
2Q	.2250	13¼	11¾	37	32½	.3125	21	18¾	—	—	—
1Q	.2250	13¼	11¼	36½	33	.3125	20¾	18½	—	—	—

*Issued August 14, 1978, upon merger of IU with C. Brewer and Company, Limited.

Officers and Directors

Senior Officers

John M. Seabrook, *Chairman and Chief Executive Officer*
John G. Christy, *President and Chief Operating Officer*
Robert F. Calman, *Vice Chairman of the Board*
John T. Jackson, *Chairman of the Executive Committee*
James J. Burke, *Executive Vice President*
John B. Turbidy, *Executive Vice President*

Operating and Staff Executives

Jack Greenberg, *Vice President, Taxes*
John B. Keenan, *Vice President, Management Resources*
Victor J. Lang, Jr., *Vice President, Government Affairs*
Edward J. Larese, *Vice President and Controller*
David W. Menard, *Vice President, Audit Services*
Walter L. Moore, *Group Vice President*
John A. Murphy, *Vice President, Corporate Development*
Laurent J. Remillard, *Vice President, Operations Analysis*
Magnus E. Robinson, *Vice President and Treasurer*
Arlen D. Southern, *Vice President, Corporate Affairs*
Anson W. H. Taylor, Jr., *General Counsel*
John J. Terry, *Group Vice President*
William H. Walker, *Secretary*
Robert W. Wolcott, Jr., *Group Vice President*

Directors

Robert F. Calman (1978), *Philadelphia, Pennsylvania*
Vice Chairman of the Board of IU
John G. Christy (1978), *Philadelphia, Pennsylvania*
President and Chief Operating Officer of IU
Lowell S. Dillingham (1978), *Honolulu, Hawaii*
Chairman of Dillingham Corporation (Diversified services company)
John T. Jackson (1971), *Haverford, Pennsylvania*
Chairman of the Executive Committee of IU
E. B. Leisenring, Jr. (1975), *Berwyn, Pennsylvania*
Chairman of Westmoreland Coal Company (Coal producing company)
Peter L. P. Macdonnell (1976), *Edmonton, Alberta*
Senior Partner of Milner & Steer (Barristers and solicitors)
Willis S. McLeese (1961), *Toronto, Ontario*
President of Trans Canada Freezers, Limited (Cold storage plant operators)
John M. Seabrook (1963), *Salem, New Jersey*
Chairman and Chief Executive Officer of IU
Lewis H. Van Dusen, Jr. (1975), *Bala Cynwyd, Pennsylvania*
Senior Partner of Drinker, Biddle and Reath (Attorneys at law)
William M. Weaver, Jr. (1958), *Smith, Nevada*
Partner of Alex. Brown & Sons (Investment bankers)
Ira T. Wender (1967), *New York, New York*
President of Becker, Warburg, Paribas Group, Inc. (Investment bankers)
The Earl of Westmorland, K.C.V.O. (1972), *London, England*
Deputy Chairman of Sotheby & Company (Fine art auctioneers)

Robert C. Heim (1958), *Briarcliff Manor, New York (Honorary Director)*
Dennis K. Yorath (1957), *Edmonton, Alberta (Honorary Director)*

(   ) Year first elected a director

New Directors and Officers

During 1978, two new directors were elected, increasing the Board's membership to 12. Elected at the annual meeting were Mr. Lowell S. Dillingham, chairman of the Honolulu-based Dillingham Corporation, and Mr. Robert F. Calman, who was elected vice chairman of IU after previously serving as an executive vice president.

Recent management changes include the promotion of Mr. Walter L. Moore to group vice president for the distribution services group. He had served for several years as president of IU's major distribution subsidiary, Unijax. Other staff appointments included Mr. John B. Keenan as vice president, management resources; Mr. David W. Menard, formerly vice president, finance, of Gotaas-Larsen, as vice president, audit services, of IU; Mr. Laurent J. Remillard, formerly an executive vice president of C. Brewer, as vice president, operations analysis, of IU; and Mr. William H. Walker, formerly assistant secretary of IU, as secretary of the corporation.

Board of Directors' Committees

December 31, 1978

Executive Committee
John T. Jackson, Chairman
Willis S. McLeese
John M. Seabrook
Ira T. Wender

Audit Committee*
Willis S. McLeese, Chairman
Lewis H. Van Dusen, Jr.
William M. Weaver, Jr.

Compensation Committee*
The Earl of Westmorland, Chairman
Willis S. McLeese, Deputy Chairman
Ira T. Wender

**All members are non-employee directors.*

The Board of Directors

The Board of Directors is elected by and is responsible to the company's shareholders. The Board directs the management of the corporation on behalf of the shareholders. In so doing, it recognizes the corporation's responsibilities to employees, customers, suppliers, and the communities and environment in which IU operates. The directors are responsible for establishing controls to ensure proper management practices, as well as appropriate and timely corporate disclosure to shareholders and government agencies.

Eight of the 12 members of IU's Board come from outside the company. They bring a wealth of experience in business, finance, world affairs, and the law, coupled with fresh perspectives and independent positions. They also broadly represent certain geographic areas in which IU and its shareholders have had a traditional interest.

Because of the need for geographical diversity, IU's directors reside halfway around the world from one another, spanning eleven time zones. These distances create special travel and communications needs. The directors keep themselves well informed about company affairs through written and telephone reports between meetings.

IU's directors are working directors. They usually devote a day and a half to each regular meeting of the Board. Eight Board meetings were held last year. There also are regular meetings of the various committees of the Board. Last year, 22 such committee meetings were held. Each committee concentrates on a specific area of Board responsibilities, enabling the Board to keep pace with the progress of IU's worldwide operations.

The directors visit key subsidiary operations periodically for reviews with subsidiary managements. This gives them first-hand knowledge of proposed major financial commitments, new facilities, and organizational problems. During 1978, Board meetings were held at Gotaas-Larsen's operations in Oslo, Norway; at C. Brewer's operations in Hawaii; and at Canadian Utilities' operations in Alberta, Canada. Each meeting included at least one full day's inspection of company facilities, such as a visit to Gotaas-Larsen drilling rigs working in the North Sea.

The dividend payout policy is determined by the Board based on earnings, cash flow, future capital requirements, and economic outlook. The dividend paid on IU's common shares has increased every year since 1944. The directors are sensitive to the shareholders' interest in IU's long-standing dividend record.

Audit Committee

The Audit Committee, composed solely of outside directors, reviews and approves the company's annual financial statements, evaluates the performance of the company's independent auditors, reviews the scope and effectiveness of IU's internal accounting and controls systems, oversees the company's response to recommendations made by the outside auditors for improvements in accounting systems, and reviews the expense accounts of the senior officers. It recommends the accounting firm to be elected by the Board for ratification by the shareholders as independent auditors for the year. The Audit Committee ensures that the independent auditors have full and free access to the committee, at times without the presence of any management representatives.

The committee meets periodically with appropriate members of IU management, the company's internal audit staff, and the outside auditors to make sure that all are executing their responsibilities, including compliance with the recently enacted Foreign Corrupt Practices Act. In 1978, five meetings of the Audit Committee were held.

In view of the international nature of IU's business, the Audit Committee is vigilant with regard to any possible irregularities such as questionable payments or political slush funds. Since 1968, when the Audit Committee was established, only one incident of a questionable payment has been uncovered. It was reported to the proper authorities, who considered it immaterial.

Compensation Committee

The Compensation Committee, established in 1964, is composed solely of outside directors. It reviews the remuneration—salary, incentive compensation, and benefits—of IU and subsidiary executives, approximately 100 in all, to insure that amounts are not only fair internally but also competitive externally. It grants stock options to key executives, and periodically reviews key executives' performance, motivation, responsibilities and remuneration. The committee provides an independent judgment on the quality of IU management, organization and personnel development, and executive performance.

The Committee retains outside independent experts to check that compensation policies are fair and equitable and that they meet the test of being appropriate and reasonable for the particular industry and country in which the service is performed. In 1978, the Compensation Committee held seven meetings.

Executive Committee

The Executive Committee's primary function is to act in the interim between regular meetings of the Board on matters that cannot be postponed until the full Board can be assembled. These matters have usually been discussed in advance with the full Board. In 1978, three meetings of the Executive Committee were held.

In addition to the above three major standing committees of the Board, there are other special-purpose committees that deal with such matters as pensions and the employee stock purchase plan. There are occasional ad hoc committees to deal with special problems. In 1978, these other committees held seven meetings.